

**INDIANA HOUSING FINANCE AUTHORITY  
MORTGAGE CREDIT CERTIFICATE PROGRAM  
THE FEDERAL RECAPTURE TAX**

The Mortgage Credit Certificate is funded from the proceeds of an IHFA Mortgage Revenue Bond. Therefore, Borrowers participating in the Program could be subject to the Federal Recapture Tax under certain conditions as discussed below.

Congress enacted legislation in 1988, subsequently amended in October 1990, to recapture some or the entire subsidy from homebuyers who receive qualified mortgage bond assistance after January 1, 1991. This includes all buyers who use IHFA mortgage loans and Mortgage Credit Certificates (MCC). The purpose of recapture was to receive the subsidy from homeowners who received rapid income increases after they purchased their home and, as a result, did not need the subsidy to remain homeowners. The Federal Recapture Tax on the mortgage under the Program is triggered when a disposition, usually a sale, of the financed residence takes place within nine (9) years of the purchase date. The amount of recapture that borrowers might have to pay depends on how much their incomes have increased, their family size at the time of sale, the original amount of the first mortgage, the length of time they owned their home and any gain realized on disposition of the home.

The borrower(s) is responsible for calculating and paying the recapture amount, if any, as additional Federal Tax Liability for the tax year in which the home is disposed. The amount of the recapture tax will not exceed fifty percent (50%) of the gain on the disposition of the home realized by the Borrower(s).

No recapture tax is due if any of the following occurs:

- (a) The borrower(s) dispose of the residence later than nine (9) years after the mortgage loan is closed;
- (b) The home is disposed of as the result of the borrower(s) death;
- (c) The Borrower transfers the home to a spouse or former spouse incident to divorce and no gain or loss was incurred on the transfer and included in his federal taxable income;
- (d) The home was disposed of at a loss; or
- (e) The Borrower(s) modified adjusted gross income for the year in which the home is sold does not exceed the threshold income adjusted for family size for such year. Modified adjusted gross income is calculated as follows:

Adjusted Gross Income from IRS 1040	\$	_____
Tax exempt income earned for the year	+	_____
Gain on sale of the home	-	_____

Modified adjusted gross income = \$ \_\_\_\_\_

There are several steps required to calculate the actual recapture amount owed. Adjustments may be made depending on the number of years the home is owned prior to disposition and the Borrower(s) income at the time of filing of the Federal Tax Return for the year of the disposition. The following outlines the steps involved in the calculation:

***Threshold income (Adjusted Qualifying Income)***

The threshold income is the maximum allowable federal income limit for the Mortgage Credit Certificate Program, for the area in which residence is located at the time the borrower was qualified for the Mortgage Credit Certificate Program. Each year of the nine (9) year holding period the threshold income is increased by 5% from the previous years' threshold income. The threshold income for each of the nine (9) years is provided to the borrower(s) in the *Notice to Borrower(s) of Maximum Recapture Tax and of Method to Compute Recapture Tax on the Disposition of Home* letter.

***Holding Period Percentage***

The percentage is based on the year in which the disposition occurs after the loan closing date according to the following table:

Disposition within month of closing:	1 - 12	20%
	13 - 24	40%
	25 - 36	60%
	37 - 48	80%
	49 - 60	100%
	61 - 72	80%
	73 - 84	60%
	85 - 96	40%
	97 - 108	20%
	109 or more	No Recapture Tax

***Maximum Recapture Amount***

The federally subsidized amount, which is 6.25%, *multiplied* times the original amount of the first mortgage, *multiplied* times the holding period percentage.

***Income Percentage***

The modified adjusted gross income of the borrower(s) for the taxable year in which the disposition occurs *minus* the threshold income *divided* by 5000.

***Adjusted Recapture Amount***

The maximum recapture *multiplied* times the income percentage.

## **Recapture**

Equals the lesser of the adjusted recapture amount or one-half the gain realized on the disposition of the residence.

### ***Limitations and Special Rules on Recapture Tax***

- (a) If you give away your home (other than to your spouse or ex-spouse incident to a divorce) you must determine your actual recapture tax as if you had sold your home for its fair market value;
- (b) If your home is destroyed by fire, storm, flood, or other casualty, there generally is no recapture tax if, within two (2) years, you purchase additional property for use as your principal residence or construct a new residence on the site of the home financed with your original subsidized mortgage loan;
- (c) In general, except as provided in future regulations, if two (2) or more persons own a home and are jointly liable for the subsidized mortgage loan, the actual recapture tax is determined separately for them based on their interests in the home;
- (d) Refinancing of the first mortgage does not result in a recapture tax liability. If the home is disposed of after the refinancing but prior to the original nine (9) year holding period recapture tax may be due. The holding period adjustment for the period in which the first mortgage was outstanding would be used for calculating the recapture amount.

Within ninety (90) days from the date of the Final Approval IHFA will send to each borrower a *Notice to Borrower(s) of Maximum Recapture Tax and of Method to Compute Recapture Tax on Disposition of Home*. A sample of this notice is included on the following pages. Borrower(s) should keep this notice for future reference in calculating the recapture tax.

## SAMPLE LETTER

**INDIANA HOUSING FINANCE AUTHORITY  
115 WEST WASHINGTON STREET  
SUITE 1350  
INDIANAPOLIS, INDIANA 46204-3413**

April 00, 2000

Orig : (Code) Bank Name (Code)  
SF #: Number LT#: Number  
Loan Amount: \$00,000.00  
Term: xx Months  
Property: Street Address  
City/Zip: City, zip  
County: County name  
Reserv/Appl Date: 00-00-00  
Commitment Date: 00-00-00  
Closing Date: 00-00-00

***Notice to Borrower(s) of Maximum Recapture Tax  
and of Method to Compute Recapture on Dispositions of Home***

In accordance with Section 143 (m) of the Internal Revenue Code, the maximum recapture tax that you may be required to pay upon disposition of this property is \$0000.00. This amount is 6.25% of the highest principal amount of this mortgage loan above referenced, and is your federally-subsidized indebtedness with respect to the loan.

Disposition Within Months of Closing	Holding Period Percentage	Adjusted Qualifying Income On date of Disposition, for Family Size	
		2 or Less	3 or More
1 - 12	20%	54,600	62,790
13 - 24	40%	57,330	65,930
25 - 36	60%	60,197	69,225
37 - 48	80%	63,206	72,687
49 - 60	100%	66,366	76,322
61 - 72	80%	69,685	80,137
73 - 84	60%	73,169	84,146
85 - 96	40%	76,828	88,352
97 - 108	20%	80,669	92,769
109 or More	No Recapture Tax		

A. ***Introduction***

1. **General.** When you sell your home you may have to pay a recapture tax as calculated below. The recapture tax may also apply if you dispose of your home in some other way. Any references in this notice to the “sale” of your home also includes other ways of disposing of your home. For instance, you may owe the recapture tax if you give your home to a relative.
  
2. **Exceptions.** In the following situations, no recapture tax is due:
  - (a) You dispose of your home later than nine years after you close your mortgage loan;
  - (b) Your home is disposed of as a result of your death;
  - (c) You transfer your home either to your spouse or to your former spouse incident to divorce and you have no gain or loss included in your income under Section 1041 of the Internal Revenue Code; or
  - (d) You dispose of your home at a loss.
  
- B. **Maximum Recapture Tax.** The maximum recapture tax amount is 6.25% of the highest principal amount of your mortgage loan and is your federally subsidized amount with respect to the loan.
  
- C. **Actual Recapture Tax.** The actual recapture tax, if any, can only be determined when you sell your home, and is the lesser of (1) 50% of your gain on the sale of your home, regardless of whether you have to include that gain in your income for federal income tax purposes, or (2) your recapture amount determined by multiplying the following three (3) numbers:
  1. The maximum recapture tax, as described in paragraph B above;
  2. The holding period percentage, as listed in Column 1 in the table; and
  3. The income percentage, as described in paragraph D below.
  
- D. **Income Percentage.** You calculate the income percentage as follows:
  1. Subtract the applicable adjusted qualifying income in the taxable year in which you sell your home, as listed in column 2 in the table on page one

of this letter, from your modified adjusted gross income in the taxable year in which you sell your home.

Your modified adjusted gross income means your adjusted gross income shown on your federal income tax return for the taxable year in which you sell your home, with the following two adjustments: (a) your adjusted gross income must be increased by the amount of any interest that you receive or acquire in the taxable year from tax-exempt bonds that is excluded from your gross income (under Section 103 of the Internal Revenue Code); and (b) your adjusted gross income must be decreased by the amount of any gain included in your gross income by the reason of the sale of your home.

2. If the amount calculated in (1) above is zero or less, you owe no recapture tax and do not need to make any more calculations. If it is \$5000 or more, your income percentage is 100%. If it is greater than zero but less than \$5000, it must be divided by \$5000. This fraction, expressed as a percentage represents your income percentage. For example, if the fraction is \$1000/\$5000, your income percentage is 20%.

#### **E. *Limitations and Special Rules on Recapture Tax***

1. If you give away your home (other than to your spouse or ex-spouse incident to divorce), you must determine your actual recapture tax as if you had sold your home for its fair market value.
2. If your home is destroyed by fire, storm, flood, or other casualty, there generally is no recapture tax if, within two years, you purchase additional property for use as your principal residence or construct a new home on the site of the home financed with your original subsidized mortgage loan.
3. In general, except as provided in future regulations, if two or more persons own a home and are jointly liable for the subsidized mortgage loan, the actual recapture tax is determined separately for them based on their interests in the home.
4. If you repay your loan in full during the nine year recapture period and you sell your home during this period, your holding period percentage may be reduced under the special rule in Section 143(m)(4)(c)(ii) of the Internal Revenue Code.

5. Other special rules may apply in particular circumstances. You may wish to consult with a tax advisor or the local office of the Internal Revenue Service when you sell or otherwise dispose of your home to determine the amount, if any, of your actual recapture tax. See Section 143(m) of the Internal Revenue Code generally.

Sincerely,

Authorized Officer